

Where a business provides repair services that are accompanied with the transfer of tangible personal property, such transactions are generally subject to tax liability under the Service Occupation Tax Act. See 86 Ill. Adm. Code 140.140(l). (This is a GIL).

May 22, 2002

Dear Xxxxx:

This letter is in response to your letter that we received on March 4, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be accessed at the Department's Website at <http://www.revenue.state.il.us/Laws/regs/part1200/>.

In your letter, you have stated and made inquiry as follows:

My client, a major truck leasing and rental company, is requesting written guidance regarding the application of sales tax to maintenance services it performs on motor vehicles.

### **Background**

My client is in the business of renting and leasing heavy-duty straight trucks, truck-tractors and semi-trailers to customers. Rentals are made to customers on a short-term basis and usually last for periods not exceeding 7 days. Leases are generally made to customers for periods of three years or more. Listed below is some background information on the specific business segments related to our ruling request.

#### *Maintenance Contracts*

My client is a major provider of maintenance contracts to lessees and owners of truck-tractors, heavy-duty straight trucks and semi-trailers. Customers typically enter into an optional agreement whereby the client performs a bundle of services for a fee. The fee can be a fixed annual amount, an agreed to per-mile driven rate, or a combination of both. Invoices mailed to customers do not contain an itemization of parts and labor consumed in the service.

In a typical agreement, my client agrees to replace worn parts, change automotive fluids, replace worn tires, and may include truck washes and other services. The client purchases all of the parts and fluids used in the performance of its maintenance contracts. The client also pays any third party service provider it uses.

Depending on the content of the agreement, customers may be billed for additional services or costs not covered by the contract. In this instance, my client will bill the customer for the services and itemize the parts and labor.

#### *Maintenance on Leased Vehicles*

My client is the registered owner of a large fleet of truck-tractors, light-duty trucks, heavy-duty straight trucks and semi-trailers that are leased to customers. Customers leasing vehicles purchase a mandatory maintenance agreement from my client. The client agrees to replace worn or defective parts, replace worn or defective tires, change automotive fluids, perform road service due to mechanical failure, and periodic exterior washing. The client purchases all of the parts and fluids used in the performance of its maintenance services. The client also pays any third party service provider it uses.

Customers may have a fixed maintenance fee included in with their monthly lease payment. Customers can also be billed a variable fee based on the amount of mileage traveled by a truck. The amount of the variable fee is itemized on the customer's invoice. Whether a fixed fee included in with the monthly lease payment or a variable fee itemized on the customer's invoice, the client does not segregate the amount of the charges related to parts and labor on the customer's invoice.

Depending on the content of the agreement, customers may be billed for additional services or costs not covered by the contract. In this instance, my client will bill the customer for the services and itemize parts and labor.

#### *Maintenance on Rental Vehicles*

The client is the owner of a large rental fleet of light-duty trucks, heavy-duty trucks, truck-tractors, and semi-trailers that are rented to customers on a short-term basis (less than 30 days). My client performs regular maintenance on the fleet in order to maintain it in good operating condition. This includes automotive fluid changes at regular intervals, replacement of worn parts, replacement of worn tires, truck washes conducted at regular intervals, and any repairs necessary to maintain the outward appearance of the vehicle.

My client purchases all of the parts and fluids used in the performance of its maintenance contracts. The client also pays any third party service provider it uses.

### **Issues**

Below is a list of questions that are itemized by business segment.

#### *Maintenance Contracts*

- 1) Is my client required to pay sales tax on the purchase of parts and automotive fluids used in the performance of optional maintenance contracts entered into with its customers, or is it allowed to claim the resale exemption? Please elaborate on your answer.
- 2) On services performed outside the contract, if my client itemized the parts and labor on the customer's invoice, can it claim the resale exemption on parts? If my

client uses a third party provider to perform maintenance services that are outside the maintenance contract, can it claim a resale exemption on the parts and labor itemized on the sales invoice mailed to the customer? Please elaborate on your answers.

- 3) Is my client allowed to purchase soap used in the performance truck washing services exempt from sales tax under the resale exemption, or must it pay sales tax to the vendor. Please elaborate on your answer.
- 4) If my client uses a third party provider for automotive maintenance services and exterior truck washing, is it required to pay sales tax to the vendor, or can it claim the resale exemption? Please elaborate on your answer.

#### *Maintenance on Leased Vehicles*

- 1) Upon the titling and registration of a leased truck, my client pays sales tax to the department of motor vehicles. Given this fact, is the client required to pay sales tax on all parts and fluids used in the performance of mandatory maintenance contracts provided to its customers, or can it claim the resale exemption? Please elaborate on your answer.
- 2) On services performed outside the contract, if my client itemizes the parts and labor on the customer's invoice, can it claim the resale exemption on parts? If my client uses a third party provider to perform services that are outside the maintenance contract, can it claim a resale exemption on the parts and labor itemized on the sales invoice mailed to the customer?
- 3) Is the client allowed to purchase soap used in the performance truck washing services for customer that have a mandatory maintenance contract, or can it claim the resale exemption? Please elaborate on your answer.
- 4) If the client uses a third party provider for automotive maintenance services and exterior truck washing, is it required to pay sales tax to the vendor, or can it claim the resale exemption? Please elaborate on your answer.

#### *Maintenance on Rental Vehicles*

- 1) The client is the registered owner of its rental fleet of trucks and trailers and pays sales tax at time of registration with the department of motor vehicles. Given this fact, can the client claim the resale exemption on its purchase of replacement parts and automotive fluids used in the maintenance of the trucks? Can it claim the resale exemption on parts and labor billed by third party maintenance providers, or must it pay sales tax to the vendor? Please elaborate on your answers.
- 2) Can the client claim the resale exemption on the purchase of soap used in the process of washing a rental truck? Please elaborate on your answer.

If you have any questions, please call me.

The taxability of maintenance agreements depends upon if charges for the agreements are included in the selling price of the tangible personal property. If the charges for the agreements are included in the selling price of the tangible personal property, those charges are part of the gross receipts of the retail transaction and are subject to tax. No tax is incurred on the maintenance services or parts when the repair or servicing is performed.

If maintenance contracts are sold separately from tangible personal property, sales of the contracts are not taxable transactions. However, when maintenance services or parts are provided under the maintenance contracts, the service or repair companies will be acting as service providers under provisions of the Service Occupation Tax Act that provide that when service providers enter into agreements to provide maintenance services for particular pieces of equipment for stated periods of time at predetermined fees, the service providers incur Use Tax based on their cost price of tangible personal property transferred to customers incident to the completion of the maintenance service. See part (3) of subsection (b) of the enclosed copy of 86 Ill. Adm. Code Sec. 140.301. Purchasers of separate maintenance agreements are not charged tax on the labor or tangible personal property that is transferred incident to the completion of the maintenance contract.

You state your client may perform repair or service work that is not pursuant to a maintenance agreement. Where a business provides repair or maintenance services that are accompanied with the transfer of tangible personal property, such transactions are generally subject to tax liability under the Service Occupation Tax Act. See 86 Ill. Adm. Code 140.140(I).

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred as an incident of their sales of service. Servicemen incur either Service Occupation Tax (SOT) liability or Use Tax liability in these transactions. The tax consequences depend upon the method used to calculate the liability. Servicemen may calculate their tax base in one of four ways: 1. Separately stated selling price; 2. 50% of serviceman's entire bill; 3. SOT on his cost price if he is a registered de minimis serviceman; or, 4. Use Tax on his cost price if he is an unregistered de minimis serviceman that is not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Please see 86 Ill. Adm. Code 140.101, the Basis and Rate of the Service Occupation Tax.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the servicemen's cost price of the tangible personal property transferred. A serviceman who incurs Service Occupation Tax on his selling price should provide Certificates of Resale to his suppliers when purchasing tangible personal property that will be transferred to service customers. Please refer to 86 Ill. Adm. Code 140.106, enclosed.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See 86 Ill. Adm. Code 140.109, enclosed. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred as an incident of the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphics arts production). Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen

should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. Such servicemen collect a corresponding amount of Service Use Tax from their customers, absent an exemption.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See 86 Ill. Adm. Code 140.108, enclosed. These de minimis servicemen do not provide Certificates of Resale to suppliers.

Your letter says that your client may use a third party provider for the performance of certain services. Please be informed that firms who do service work for customers of another business are sometimes secondary servicemen in multi-service situations. Multi-service situations exist where a primary serviceman subcontracts work to a secondary serviceman. See 86 Ill. Adm. Code 140.145 for information about multi-service situations.

In multi-service situations, a primary serviceman's cost price is determined either by the separately stated selling price of the tangible personal property transferred from a secondary serviceman, or if the secondary serviceman does not separately state the cost of goods, it is presumed that the primary serviceman's cost price is 50% of the secondary serviceman's total charge. See 86 Ill. Adm. Code 140.301(a).

When both primary servicemen and secondary servicemen are registered, primary servicemen may give a Certificate of Resale to registered secondary servicemen for any tangible personal property purchased. See Section 140.145(c). Primary servicemen could then collect Service Use Tax from their customers based upon the separately stated selling price of the property or 50% of the bill to the service customers.

If primary servicemen are registered and de minimis, they may choose to remit Service Occupation Tax to the Department based upon their cost price of tangible personal property purchased from secondary servicemen. It shall be presumed that the cost price to the serviceman of the property transferred to him by his or her subcontractor is 50% of the total bill from the secondary serviceman in the absence of proof of the consideration paid by the subcontractor for the purchase of such property. Registered de minimis primary servicemen provide the secondary servicemen with Certificates of Resale if the secondary servicemen are registered, and collect Service Use Tax from customers on their cost price.

Please be advised that the Illinois General Assembly enacted legislation that provides for multi-service situations that involve unregistered de minimis servicemen. Public Act 89-675, effective August 14, 1996, states that if an unregistered de minimis serviceman subcontracts service work to an unregistered de minimis secondary serviceman, the primary serviceman does not incur a Use Tax liability if the secondary serviceman (i) has paid or will pay Use Tax on his or her cost price of any tangible personal property transferred to the primary serviceman and (ii) certifies that fact in writing to the primary serviceman. See Section 140.145(a). This certification option is only available in multi-service situations when both the primary and secondary servicemen are unregistered and de minimis, 35 ILCS 110/2 and 115/2.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at [www.revenue.state.il.us](http://www.revenue.state.il.us). If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

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Associate Counsel

KWB:msk  
Enc.